

## **WestJet Is Our People –** **FAA Washington**

Good morning ladies and gentlemen.

It is a pleasure for me to be able to come to address you for the first time in Washington and be able to talk to you from the perspective of a low fare growth carrier like WestJet. I would like to take some time talking about WestJet, the history behind our airline, who we are, what we do, our corporate strategy, some of our successes, the future of the Canadian airline industry and the future of WestJet. For those of you who may not be that familiar with the WestJet story, I'd like to tell you a little bit about us.

In 1994, Clive Beddoe, who was at that time, and currently still is, President of the Hanover Group of Companies, bought a company that required him to travel weekly between Calgary and Vancouver. Clive, being a recreational pilot, determined that it was cost effective to purchase his own aircraft, to make the weekly commute, as opposed to paying the \$800.00 it cost him to fly between the two cities on the major airlines. When that aircraft was not being used, it was available for charter with other companies. Very quickly it was being utilized heavily. At the same time, Mark Hill, our current VP, Strategic Planning, having the opportunity of flying around the United States, found that there were carriers in that country, who were able to charge fares at less than half what the major airlines were able to charge, provide great service, and most importantly of all, provide a tremendous return for their shareholders.

In August 1994, a business plan was put together by Mark, which showed that the same concepts as employed by SouthWest Airlines should be successful here in Western Canada. As a result on February 29, 1996, with 3 owned aircraft, 220 employees, and with service to five cities, WestJet took flight. We now have over 1100 employees, 14 aircraft, serve 12 cities in Western Canada and in 1999 carried well over 2 million passengers. We have carried 5 million passengers since we started.

It is a success story in an industry, where success stories are very rare, and a success story that is a credit not to the financiers or to the management of this company, even though they have done a fabulous job, but rather to the people of this company, otherwise known as our employees.

WestJet employs what I would call a "market driven strategy", that is, we looked at our market, designed our plan and designed the company around the market requirements. Actually that is a fairly academic term to what we did. The reality is that we looked at our friends SouthWest, took along a very good copier, and mimicked a lot of what they were doing. SouthWest, who is probably the most

successful carrier in the United States, the most consistently profitable and with the most consistent growth, has a number of basic tenants to its strategy. Primarily, it grows a market place, by offering short haul air transportation, and stimulates that market, as opposed to playing the market share game. That business philosophy was 100% adopted by WestJet, when we began to design our airline. That is, we believe we can stimulate air transportation on short haul markets, where our primary competition is the car, the bus, and the train. In addition we believe we can compete for the discretionary entertainment dollar, from individuals who would otherwise have spent weekends, or weekdays, at home, at movies, in restaurants – or in some cases the bar. When you look at this market segment, what factors would you have to put in place in order to do this?

First the airfares would have to be low, extremely low, to compete, particularly with the car. Second, since no one ever bought a Lada car twice, while the airfares would have to be much lower than the prevailing airfares, there would have to be tremendous value for the customer's air transportation dollar. One of the tenants behind our company, is we believe the air transportation industry is a customer service business first, and operational business second, where most airlines believe the exact opposite.

When I look 20 years into the future, what is going to differentiate WestJet from any other carrier? Any one can go out there and buy 737s. Anyone can fly between Calgary and Vancouver, anyone can leave and arrive at the same time as us, and anyone can charge the exact same fares as us.

What is going to differentiate WestJet from all other airlines? Our Customer Service: So, if going in, the two tenants for the company are going to be price of the airfares, and the customer service, how do you get both of these aspects in line with your market driven strategy? Well, that is very easy. It is in the people that you hire for your company.

People can give you the cost base on which you can charge the low fares, and people are the only ones that can give you the customer service. The next natural question is how can we charge fares that in many cases are less than half of what the national airlines are charging? Well there are a number of factors. First, as I indicated our people are key, we currently average 65 employees per aircraft, which would compare between 145 and 170 for the national airlines. Second, the operation of one aircraft type. The 737-200 has tremendous economies of scale, particularly in terms of pilot training, maintenance training, and spares. Third, fuel is another area in which we at WestJet feel we are not experts, and thus have hedged ourselves on an ongoing basis. Currently our fuel costs are an equivalent of \$16.00 US per barrel and

have recently entered into another hedge, which will carry us to June 2003, at an equivalent rate of \$18.00 US per barrel, although our contract is in CDN dollars.

This obviously compares very favorably with today's price of over \$30.00 US per barrel that the spot market is demanding, and which appears to be rising, and validates our premise that we are experts in the airline industry, but not in the oil industry, or currency fluctuations. Fourth, in addition to the above, we do not have a frequent flyer program, participate in Computer Reservation Systems, have first class lounges, or serve meals on board our flights. As our average flight is approximately one hour, there is little or no requirement from our guests for such amenities. In fact what we hear from our guests is "keep the price low and we will fly with you", which is a far cry from the heady days of the 80s, in which the mantra used to be "give us more and we will pay you more", which has led to the high cost overhead situations that we see at the other carriers.

## **PEOPLE:**

One natural question at this point will be "Well, how do you motivate the people at WestJet?" What sort of salaries do you pay and why are you able to be so productive when the other airlines aren't? I will say, in the other company's defense, it is much easier starting off with a blank piece of paper than inheriting a corporate culture that is some 50 years old. That having been said, I believe that WestJet is a model for companies looking to achieve their business objective, because there are very few industries where you can achieve any sort of corporate objective without having your people aligned with the success of the corporate goals. There are two areas in which a company has a relationship with its people. The first is in terms of how you work with them, the second is financially and I will tell you the two areas must be aligned otherwise, neither area will work well and that relationship will be destroyed.

If you go back to Psychology 101, there are certain consistent facts about people that a company must recognize and this goes for every person. People want to feel that they contribute. People want to feel that they are recognized when they do a good job. People want to know they are valued. People want to know that their input is not only considered, but also needed. People want to have a say in the company they are working with. I believe that even outside the airline industry, these are consistent requirements of any human being, and we at WestJet agree. As a result, we have focused our total management team on working with our people. We believe that by working with our people, in this sort of manner, and focusing upon them as individuals, we will achieve our corporate goals as I indicated earlier. When I say we value our people, we do not call them employees, but as you may have noticed, rather they are "people" who work with our airline and therefore have adopted this name.

As well we call our customers, or our passengers, as they are known corporately in the airline industry, our "guests," because this sends a very subtle, yet strong message to everyone in our airline, as to the type of treatment they, and we, expect they will be accorded. First though, one of the most important aspects of WestJet is we have to hire right and are constantly looking for people who embody what we consider to be the WestJet corporate spirit. That is the friendly "can do" attitude that we believe everyone at WestJet has. We have an agreement with our people, that we will pay 95% of the median salaries of the regional airline industry or of the industry in general. This means the average WestJet employee is slightly below the median wage of comparable jobs in our industry. However in return, WestJet has a profit sharing program. In November, we handed out \$3.7M of profit sharing to our people for a six-month period, which represented approximately 30% of salaries for the same period. In addition WestJet has an employee share purchase program, where we match dollar for dollar, investments made by our people up to 20% of their gross salary, which is a very generous program. Through this financial package, we once again have aligned the interests of our employees with the interests of the company. In this scenario I believe everyone wins. While I am very excited to come to work everyday, I believe it is through the people at WestJet that make that excitement possible and as a result acknowledge them whenever we talk about the success of our airline.

There are many people who believe that if they pay less for a product they are in fact getting less. Let me tell you that once again, this is not the situation with WestJet, which embodies friendly, down home customer service with the operational integrity of its airline, which is paramount, if we truly are going to offer the product, which is requested by customers.

That is – on time flights, particularly on the short haul flights where time is of the essence. I will also tell you that WestJet is renowned for it's operational performance and year to date, including the winter months, has cancelled on average five out of every one thousand flights, which is a phenomenal feat in the airline industry where most regional carriers will cancel five in every on hundred flights or 10 times as many. In addition, our on time performance of the flights which we do operate is second to none in the airline industry where our on time arrivals (within 15 minutes) is at 92.2% which is a leading indicator in our industry. In addition our aircraft are spotless, which any of you who have flown with us can attest to. The seat pitch in our aircraft, or the distance between the seats is equal to the seat pitch in the economy class in Air Canada and Canadian and far ahead of the standard seating configuration of the charter aircraft.

## **SUCCESS:**

All this is translated into an extremely successful company and, yes, extremely successful airline as well. As of September 1999, we had a shareholder's equity of almost \$90M, up from \$47M last year. We had generated \$137M worth of revenue, compared to \$83M last year and had net earning of \$11.1M versus earnings of \$4.8M last year. With the help of our travel agency partners, we have filled 72.6% of our seats compared with 71.2% last year. Our capitalization, based upon our current stock price is now \$500M, which, for a company that is only 4 years old, operating 14 aircraft, is quite a feat. Most importantly I believe we are perceived as being the airline of choice in western Canada, if we judge by the accolades we receive on a daily basis. Which is probably our most important litmus test of our success.

So what is the future of the Canadian airline industry and how does WestJet fit in? When I take a look forward, and look at what has happened in the Canadian airline industry, specifically that of the purchase of Canadian Airlines by Air Canada, I see the industry becoming slightly different in the future. In the past, the splitting of the traveling public was done by two airlines that basically went after the same passengers with the same products, with the same service.

They basically split the traveling public on a vertical basis. Now, I believe there will be a bifurcation of the airline industry. For those of you who don't know what this word is, and I didn't either, until about three months ago, bifurcation means splitting in two. I believe the airline industry will be bifurcated horizontally, meaning that there will be a group of passengers, and if we look at the group of passengers as being a box, they will be split horizontally.

The top end of the box, will be those passengers who want net work connections, for example, to Shanghai. They want frequent flyer points. They want business class. They want first class lounges.

The bottom group is passengers who basically would sit home, would drive, would take the bus or otherwise not move if the fares weren't low enough. I see this line being drawn, and there are a group of passengers, those who as companies may become price sensitive and on the other side we have passengers, who, if the time is not right are willing to pay more. I see the industry being bifurcated between Air Canada and WestJet on a price point as opposed to both airlines being all things to all people.

Air Canada has indicated that they will be consolidating capacity between Air Canada and Canadian reducing their domestic services by at least 15%. We believe that these primary reductions are in the short haul marketplace. As a result this will give more opportunities for WestJet's services to expand even further than we have already.

On average in 1997, which is only two years after we started, versus 1995, which is before we started, we have stimulated the average market place over 150% according to Stats Canada figures. I believe this number is probably closer to 250% on average, which shows that the SouthWest/WestJet phenomena of offering low prices on short haul routes has a very powerful stimulus factor and is really creating its own market place, as opposed to going after someone else's. We are able to stimulate this market place because our walk up fares are less than 40% of those charged by the main line carrier, and in addition our advance purchase tickets do not have a Saturday night stay over requirement.

Our vision as an airline is to become Canada's low fare, short haul air carrier. In order to bring us closer to that vision, we will be starting service into Hamilton's John C. Munro Airport on March 8<sup>th</sup>, with service from Winnipeg and Thunder Bay, with one stop service through to Calgary. On April 19<sup>th</sup> we will be adding service to Moncton and in the early summer to Montreal and Ottawa, as well as increased frequencies to all of these destinations. This is a very bold move on our part, but one that was developed as a result of a window of opportunity presented to WestJet as the result of the purchase of Canadian Airlines by Air Canada and resulting agreement which prohibited Air Canada from starting a low cost carrier in Hamilton until September of 2000 if WestJet started service, or September, 2001 if any other carrier started service. As far as service to Ottawa is concerned, we will start service to and from Hamilton, which really services southern Ontario. Hamilton, is a very interesting airport. It services 2.2M people.

That of course, is only the beginning. We felt that Western Canada could take 30 – 40 aircraft. We believe that Canada could take upwards of 100 aircraft, giving us tremendous opportunities, even prior to looking at the U.S.

We have signed a memorandum of understanding with Boeing for up to 70 new generation aircraft to replace our current fleet of 737-200's.

After all the strategy, the ideas, and the design of the airline, the reality is the operation and delivery of the WestJet product comes down to one key factor, and one key factor only, and that is our people. They are what have got us to where we are. They are what will take us to where we are going to be.

This is a growth company. I look forward to being along on the trip with them and look forward to seeing you on board WestJet sometime soon.

Thank you.